Raising Funds in International Markets – RIL Bonds

During the financial year 1996-97, RIL raised US $300 million\(^1\). The maturities for these issues were right across the yield curve, ranging from 10 to 100 years. RIL became the first private sector company to raise such a huge amount of funds without a bank guarantee. According to analysts, the high investment grade ratings obtained from international rating agencies had provided comfort to lenders vis-a-vis Reliance’s creditworthiness.

ABOUT THE COMPANY

RIL, a Fortune Global 500 company, was from the Reliance Group (a highly diversified conglomerate which had businesses in the energy and materials value chain) and was the largest private sector company in India. As of 2010, RIL’s annual revenue was in excess of US$ 34 billion. Backward vertical integration had been the cornerstone of the evolution and growth of Reliance. Starting with textiles in the late seventies, Reliance pursued a strategy of backward vertical integration — in polyester, fiber intermediates, plastics, petrochemicals, petroleum refining, and oil and gas exploration and production — to be fully integrated along the materials and energy value chain. The Group’s activities spanned exploration and production of oil and gas, petroleum refining and marketing, petrochemicals (polyester, fiber intermediates, plastics and chemicals), textiles, retail, and special economic zones. Reliance enjoyed global leadership in its businesses, being the largest polyester yarn and fiber producer in the world and among the top ten producers of major petrochemical products. The Group exported products in excess of US$ 20 billion to 108 countries in the world. Major Group companies were Reliance Industries Limited (including main subsidiaries Reliance Petroleum Limited and Reliance Retail Limited) and Reliance Industrial Infrastructure Limited.

RIL BONDS

In the financial year 1995-96, Reliance became the first private sector company in India to be rated by international credit rating agencies. Three US-based international rating agencies — Standard and Poor’s (S&P), Moody’s, and The National Association of Insurance Commissioners (NAIC) — rated Reliance during the year. S & P rated Reliance “BB+, Stable Outlook, constrained by the Sovereign Ceiling”, Moody’s rated it “Baa3, Investment Grade, constrained by the Sovereign Ceiling” and NAIC rated it “NAIC 2, Investment Grade” — against the background that international rating agencies generally did not rate a company higher than the country in which it

\(^{1}\) Reliance Industries Annual Report 1996-97

This case study was written by R Muthukumar, IBS Hyderabad. It is intended to be used as the basis for class discussion rather than to illustrate either effective or ineffective handling of a management situation. The case was compiled from published sources.

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was domiciled. The leading Indian rating agency, Credit Rating and Information Services India Limited (CRISIL), S & P’s Indian associate, assigned an “AAA” rating to Reliance’s long-term credit, signifying “Highest Safety”. These ratings enabled Reliance to raise US$ 300 million\(^2\) in the international debt market in two landmark transactions in 1995. Reliance became the first Indian private sector company to raise US$ 150 million as a 7-year syndicated bullet loan at a floating rate of LIBOR plus 1%, and to issue 10-year bonds of US$ 150 million in the US market, without any guarantee or security from banks, financial institutions, or the government. These transactions assisted Reliance in reducing the overall cost of capital at a time when the money market conditions in India were stringent. These transactions were also consistent with the conservative financial policy adopted by the company.

During the financial year 1996-97, Reliance tapped the US debt market with its five Yankee Bond issues for a total sum of US $614 million\(^3\). The maturities for these issues were right across the yield curve, ranging from 10 to 100 years (Refer to Table I for ‘Bonds issued by Reliance during 1996-97’).

**Table 1**

<table>
<thead>
<tr>
<th>Time of Issue</th>
<th>Amount in US $ (mn)</th>
<th>Maturity</th>
<th>Option (if any)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jun-96</td>
<td>100</td>
<td>20</td>
<td>none</td>
</tr>
<tr>
<td>Jun-96</td>
<td>100</td>
<td>30</td>
<td>put 12 yr</td>
</tr>
<tr>
<td>Aug-96</td>
<td>100</td>
<td>50</td>
<td>put 30 yr</td>
</tr>
<tr>
<td>Jan-97</td>
<td>214</td>
<td>30</td>
<td>put 10 yr</td>
</tr>
<tr>
<td>Jan-97</td>
<td>100</td>
<td>100</td>
<td>none</td>
</tr>
</tbody>
</table>

*Source: Reliance Industries Annual Report 1996-97*

With these issues, Reliance achieved the following in the global capital market:

1. Was the first corporate issuer of 50- and 100-year bonds from Asia.
2. Was the first issuer with split rating (due to the constraint of India’s sovereign rating) in the world to issue a 100-year bond.
3. Was among the 30 issuers in the world who had accessed the 100-year market from 1992 to 1996.
4. By 1996-97, Reliance had 10-, 12-, 20-, 30-, 50-, and 100-year bonds outstanding and thus provided a benchmark yield curve for future Indian issues.

**INTERNATIONAL DEBT ISSUES – BENEFITS**

Till March’97 Reliance had raised a total of US $ 914 million in the international fixed income market. This led to a lowering of its average cost of capital and increase in the average maturity. The average maturity of debt more than doubled, thereby bringing the maturity profile closer to the

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\(^2\) Reliance Industries Annual Report 1995-96

\(^3\) Reliance Industries Annual Report 1996-97
economic life of the underlying productive assets. The average maturity of the total foreign debt of Reliance went down to 23 years\(^4\).

Market access was at a time of historically low interest rates, which led to further savings in interest cost. With this, Reliance became a well-known name in the international capital markets with the ability to raise funds at competitive cost.

During the financial year 1997-98, the company refinanced its US $150 million syndicated loan, and obtained the tightest pricing for any Indian private sector company. It issued sterling notes for 150 million which were by and large placed with institutional investors in the UK. It also made a US $150 million\(^5\) private placement of notes to European banks and institutional investors. The company demonstrated its financial flexibility during 1997-98 by successfully tapping the domestic debt markets, when international markets remained closed to most issuers from emerging markets on account of the Asian economic crisis. During the year, it privately placed debentures of US $272 million to finance ongoing capital expenditure. It also raised nearly US $47 million by issue of preference shares, the largest issue of preference share capital from any private sector company in India. During the year, the company made an early redemption of three series of public debentures, aggregating to US $164 million. The rating of the company’s long-term debt from CRISIL was maintained and reaffirmed at AAA, the agency’s highest rating.

Foreign currency denominated investments and balances as on March 31, 1999, stood at US $1.3 billion\(^6\). These offered the company a substantial hedge against translation risk on its long-term debt. The company believed that any adverse effect of devaluation of the rupee on its results was unlikely to be significant, in view of several factors such as the holding of significant foreign currency denominated investments and balances, increasing export revenues, the dollar-based, product selling pricing strategy adopted by the company, and the hedging transactions undertaken by the company. Reliance undertook liability management transactions, such as interest rate swaps and currency swaps, on an ongoing basis, to reduce the overall cost of debt and diversify its liability mix.

QUESTIONS FOR DISCUSSION

1. Discuss the fund raising strategy adopted by RIL for raising funds from international markets. What innovative approaches did it employ?
2. How did RIL succeed in raising funds from the US market without any bank guarantee?
3. How did RIL refinance its syndicate loan?
4. Compare the rates at which RIL was able to raise funds with other companies of similar size in India and abroad.

PROBLEM SET

As shown in Table 1, the company raised $100 million through a 30-year bond (F.V.=$100) with a coupon rate of 10%. At the time of bond issue, the company’s other bonds with different maturity also traded in the market. Answer the following questions related to this bond issue:

\(^4\) Reliance Industries Limited Annual Report 1996-97
\(^5\) Reliance Industries Limited Annual Report 1997-98
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Q1 Ascertain the cash outflows for the bond till their maturity.
Q2 If the YTM in the market for a 30-year bond is 10%, compute the price of the bond? What is your inference?
Q3 If, after the issue, the interest rates dropped by 1% then what would be the price of the bonds? The bond would trade at ________ to the face value.
Q4 If, after the issue, the interest rates rise by 1% then what would be the price of the bonds? The bond would trade at ________ to the face value.
Q5 What principle of bonds pricing do you infer from the results of Q3 and Q4?

Q6. Just after the issue, the interest rates dropped by 1%. What is the current yield of the bond? What is the YTM? What if after the issue the interest rates for the bond rise by 1%? What do you infer?
Q7 Compute the present value of the bond at different points in time (n=5, 10, 15, 20, 25, 30) till the maturity of the bond when interest rate drops by 1% after the issue.
Q8 Compute the present value of the bond at different point in time (n=5, 10, 15, 20, 25, 30) till the maturity of the bond when interest rate rises by 1% after the issue.
Q9 From the results of Q7 and Q8, we infer that the ________/_________ on the bond ________as the bond approaches maturity.
Q10 One of the other RIL bonds of 10-year maturity (F.V.=Rs.100, coupon rate=10%) is also trading in the market at a yield of 9% while the 30-year RIL bond is trading at a yield of 10%. What is the percentage change in price for each of these bonds for a 1% decrease in the yields across all maturities?
Q11 What is the percentage change in price for each of these bonds for a 1% increase in the yields across all maturities?
Q12 What would you infer from the sensitivity of different maturity bonds for a given change in yield?
Q13 In the example given, for the RIL 30-year bond, when interest rate falls by 1%, what is the % change? What is the % change when the interest rates rise by 1%? What is your inference?
Q14 (Assume that) RIL issued a 40-year bond 10 years before the issue of this 30-year bond at a coupon rate of 11% (F.V.=1000). The yield in the market for the 30-year RIL bond is 8%. If the yield for 30-year maturity drops by 1%, then what is the % change in price for these different 30-year bonds?
Q15 What is the % change for the yield for 30-year maturity rises by 1%?
Q16 What inference can you draw about the change in bond price for similar maturity bonds with different coupon rates?